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## RESEARCH REPORTS

### COMING EFFECTS OF CURRENT EVENTS

#### *The Federal Budget*

The budget message presented by the President to Congress on January 21, 1954, was the first budget initiated by the present Administration and the first Republican budget since 1929.

#### *Estimated Budget Expenditures in Fiscal 1955*

The budget for fiscal 1955 (year ended June 30, 1955) reflects a partial fulfillment of pre-election promises that Federal expenditures would be cut sharply and that the budget deficit would be brought under control. The proposed Government expenditures of \$65,570,000,000 during fiscal 1955 are about \$4,300,000,000 less than those estimated for fiscal 1954 and about \$8,700,000,000 less than those during fiscal 1953, when the postwar peak of Federal expenditures was reached.

About 69 percent of all expenditures during fiscal 1955 is scheduled to be spent for defense and defense-related purposes, such as foreign military aid and atomic research. Direct military expenditures for the Army, Air Force, and Navy are estimated at \$38,160,000,000, compared with \$42,320,000,000 during fiscal 1954 and the postwar high, \$44,520,000,000, during fiscal 1953. Substantial savings in military expenditures are said to have resulted from " \* \* \* revisions in programs, from shifts in emphasis, from better balanced procurement, and from improved management and operations." The revisions in programs and shifts in emphasis are toward the "creation, maintenance, and full exploitation of modern air power" and toward improvement of "combat effectiveness of our forces by the application of new weapons and new techniques." These contemplated shifts are reflected in the following table.

	Actual 1953		Estimated 1955	
	Billions of Dollars	Percent	Billions of Dollars	Percent
Army	\$16.24	32.2	\$10.20	22.8
Navy	11.87	23.6	10.49	23.4
Air Force	15.09	30.0	15.21	36.2
Foreign Military Aid	3.95	8.0	4.28	9.6
Atomic Energy Expenditures	1.79	3.6	2.13	5.4
Other	1.33	2.6	1.18	2.6
<b>Total</b>	<b>\$50.27</b>	<b>100.0</b>	<b>\$44.79</b>	<b>100.0</b>

Substantial reductions in expenditures for the Army are supposed to have been made possible as a result of decreased outlays for the procurement and production

of military equipment as well as by reductions in military personnel from 3,400,000 men to 3,000,000 men by June 30, 1955. Although the number of men under arms will be reduced substantially, the " \* \* \* increased mobility and the availability of modern weapons will provide each division with increasingly greater striking power."

Procurement expenditures for the Air Force and the Navy are expected to be maintained during fiscal 1955 at a level nearly equal to that during fiscal 1954. The total active aircraft of the Air Force, Navy, and Marine Air Force is scheduled to be increased from 33,000 units to approximately 40,000 units in the next 3 years, half of which will be jet aircraft.

The substantial increase in expenditures for atomic-energy research and production to \$2,430,000,000 during fiscal 1955 is attributable to the rise in operating costs of newly completed plants and to continued capital expenditures for previously authorized new construction.

#### SUMMARY OF THE NATIONAL BUDGET (Billions of Dollars)

	Fiscal Year 1940	Fiscal Year 1953	Fiscal Year 1954 (Est.)	Fiscal Year 1955 (Est.)
<i>Accounts</i>				
Receipts:				
Direct Taxes on Individuals	\$ 1.34	\$33.37	\$34.39	\$31.28
Direct Taxes on Corporations	1.27	21.60	22.81	20.26
Excise Taxes	1.88	9.99	10.23	10.24
Employment Taxes	.84	4.99	5.53	6.42
Customs	.35	.61	.59	.59
Miscellaneous Receipts	.27	1.86	2.31	2.45
Deduct: Refunds and Old-Age Insurance Appropriations	-.09	-7.83	-8.23	-8.60
<b>Total Receipts</b>	<b>\$ 5.86</b>	<b>\$64.59</b>	<b>\$67.63</b>	<b>\$62.64</b>
Expenditures:				
National Defense	\$ 1.50	\$44.52	\$42.32	\$38.16
Foreign Mil. and Ec. Aid	.05	5.91	5.76	5.30
Atomic Energy Commission	....	1.79	2.20	2.43
Interest on Public Debt	1.04	6.50	6.53	6.80
Other Activities:				
General Government	.34	1.44	1.18	1.16
Transportation and Communication	.53	2.08	1.86	1.42
General Public Works	.63	1.91	1.23	.82
Veterans' Services and Benefits	.55	4.30	4.16	4.19
Aid to Agriculture	1.57	2.94	2.65	2.37
Social Security Programs	3.15	1.91	1.95	1.81
Labor	.01	.28	.27	.28
Miscellaneous	.08	.40	.79	.83
<b>Total Expenditures</b>	<b>\$ 9.45</b>	<b>\$73.98</b>	<b>\$70.90</b>	<b>\$65.57</b>
<b>Surplus (+) or Deficit (-)</b>	<b>-3.59</b>	<b>-9.39</b>	<b>-3.27</b>	<b>-2.93</b>

Foreign military and economic assistance is estimated to decrease slightly from \$5,760,000,000 during fiscal 1954 to \$5,300,000,000 during fiscal 1955. Economic aid to Western European countries will decrease; technical aid to Asia, Africa, and Latin America will increase. Foreign economic and technical aid will be slightly more than \$1,000,000,000, compared with \$4,275,000,000 for military assistance.

Interest payments on the public debt are expected to increase \$270,000,000 to \$6,800,000,000 during fiscal 1955. Higher average interest rates and a larger debt are expected by the Administration.

Expenditures for all other governmental activities, such as transportation and communication, veterans' services, aid to agriculture, public works, etc., will decrease by \$1,200,000,000. Primarily responsible are the scheduled decreases in post-office expenditures (\$350,000,000) and in expenditures for general public works (\$400,000,000). The latter decrease is unusually significant in view of widespread rumors that the Administration has been contemplating increasing public works in the event of a more severe recession.

#### *Estimated Budget Receipts in Fiscal 1955*

Budget receipts during fiscal 1955 are estimated at \$62,642,000,000, about \$5,000,000,000 less than those during fiscal 1954. Direct taxes on individuals are expected to decrease by \$3,000,000,000 and those of corporations by \$2,500,000,000. The revenue decrease seems to be largely attributable to the individual-income-tax reduction of 11 percent and the elimination of the corporate excess-profits tax.

Other tax-revenue estimates have been made under the assumption that Congress will enact the President's proposals to defer reductions in corporate income-tax rates and in the excise tax on liquor, tobacco, automobiles, and gasoline.

Some decrease in total personal income during 1954 and early 1955 apparently is expected by the Bureau of the Budget. However, corporate-income-tax receipts are estimated on the basis of profits for 1954, which were assumed by the Administration to be equal to those during the third quarter of 1953. Because profits during 1954 probably will be lower than this estimate and because of the probability that Congress will not approve all the President's recommendations for extension of present tax rates, the fiscal-1955 receipts estimates may prove to be somewhat optimistic.

#### *Balancing the Budget*

Although expenditures would be reduced substantially in fiscal 1955, a balanced budget apparently would not be achieved either in fiscal 1954 or in fiscal 1955. According to the message, the budget deficit during fiscal 1954 will be \$3,270,000,000 and during fiscal 1955, nearly \$3,000,000,000. The expected deficit in 1954 has been decreased substantially from the \$9,900,000,000 estimated by President Truman in the 1954 budget message.

As readers may realize, the Federal cash budget (which includes receipts and expenditures of Federal trust funds) rather than the administrative budget discussed above is more revealing in estimating the inflationary or deflationary impact of Government fiscal activities. According to the President's estimates, the cash budget for fiscal 1954 would result in a net cash deficit of only \$200,000,000, substantially less than the earlier estimate of \$6,400,000,000. During fiscal 1955 a net

surplus of \$100,000,000 is expected in the cash budget. Thus, during both fiscal 1954 and fiscal 1955 the Federal Government's fiscal operations would not contribute significantly either to inflation or to deflation.

Smaller military expenditures (assuming no major change in the international situation) during fiscal 1956 or even 1957 will tend toward a balanced administrative budget. On the other hand, enactment of some of President Eisenhower's welfare programs and increasing benefits in the future may counterbalance the decreased defense expenditures to some extent. Moreover, the desire on the part of both the public and the Government to have taxes reduced as soon and as much as possible may result in a decrease in Federal revenues that could reverse the trend toward a balanced budget.

#### *Proposed Fiscal Legislation*

In his budget message the President renewed his request to Congress to raise the public-debt limit because "in view of the wide swings in receipts and expenditures and their unpredictability, it is not prudent to operate the huge business of the United States Government in such a strait-jacket as the present debt limit."

He proposed 25 revisions in the tax structure. The more significant ones are as follows:

1. To regard a child as a dependent regardless of the child's earnings.
2. To allow widows and widowers with dependent children to split their incomes as is now done by married couples.
3. To permit a tax allowance for medical expenses in excess of 3 percent of income instead of the present 5 percent.
4. To decrease the double taxation of dividends.
5. To calculate the annuity tax on the basis of the life expectancy of the person receiving it.
6. To shift the deadline for filing income-tax returns from March 15 to April 15.
7. To allow more extensive use of straight-line depreciation of business capital equipment.
8. To permit expenditures for research and development to be deducted for tax purposes.
9. To tax income from foreign subsidiaries at a rate 14 percentage points lower than the regular corporate rate.
10. To shift corporate income-tax payments by requiring payments based on advance estimates in September and December prior to the end of the taxable year.

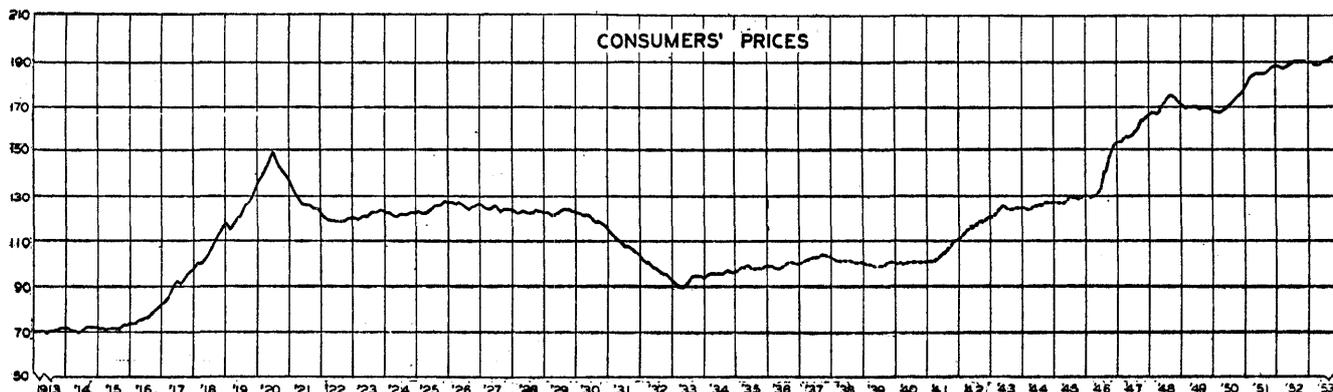
#### *Conclusions*

*Estimates of the cash budget during fiscal 1954 and fiscal 1955 suggest that Government fiscal activities will have little inflationary or deflationary effect. Present tax legislation, under which a major portion of tax payments are to be made during the first half of the year, probably will result in some inflation during the latter part of 1954 and a counterbalancing deflation during the early months of 1955. The President's proposal to advance corporate income-tax payments would contribute somewhat toward smoothing out these "seasonal" inflationary and deflationary fluctuations.*

### **Summary Comments on Recent Developments**

#### *Russian Gold*

Readers of our bulletins and other individuals have expressed concern over the recent shipments of Soviet



gold to England in exchange for goods. Thus far the Institute does not believe that there is much reason for concern about Russia's actions. Estimates of the gold involved vary from \$100,000,000 to \$200,000,000 worth, an amount that is relatively insignificant when compared with the outflow from the United States of approximately \$1,000,000,000 during the past year.

#### *Social Security Solvency*

The President's discussion of the social-security program was devoted primarily to possible ways of expanding coverage and increasing benefits. The longer term financial considerations were ignored. Those disturbed about the long-term financing of the program were assured that "the benefit costs will be met for at least the next fifteen to twenty-five years under the step-rate increases in O.A.S.I. taxes already provided in the law."

#### *The Randall Report*

The Randall Commission report on United States Foreign Economic Policy appeared to be a step in the direction toward "freer" trade. The published excerpts provided little to indicate the reasoning on which the findings and recommendations were based, but extension of the Reciprocal Trade Agreements Act and the authorization of at least 5-percent reductions in tariff rates during the next 3 years suggest that there was some understanding of the benefits of "free" trade.

## SUPPLY

### *Industrial Production*

Steel-ingot production, scheduled at 73.8 percent of capacity for the week ended January 30, 1954, was slightly less than that in the preceding week but was 21 percent less than production in the corresponding week last year.

	1929	1932	1937	1938	1953	1954
Percent of Capacity†	85	27	76	33	99	74p
Weekly Cap. (Million Tons)	1.38	1.52	1.51	1.54	2.25	2.38
Production (Million Tons)	1.17	.41	1.15	.51	2.23	1.76

Automobile and truck production in the United States and Canada during the week ended January 23, 1954, was estimated at 151,827 vehicles, compared with a revised total of 149,601 vehicles during the previous week.

	1929	1932	1937	1938	1953	1954
Vehicles (000 omitted)†	107	30	81	65	150	152p

Electric-power production in the week ended January 23, 1954, decreased to 8,976,000,000 kilowatt-hours from 9,013,905,000 kilowatt-hours in the previous week.

	1929	1932	1937	1938	1953	1954
Billion Kilowatt-Hours†	1.72	1.60	2.29	2.16	8.14	9.00

Lumber production in the week ended January 16, 1954, increased. *The New York Times* seasonally ad-

justed index was 7 points above that for the preceding week but was 13 points below that for the corresponding week last year.

	1929	1932	1937	1938	1953	1954
<i>The New York Times</i> Index†	145	39	96	75	144	131

†Latest weekly data; corresponding weeks of earlier years  
p=preliminary

## DEMAND

### *Department-Store Sales*

Department-store sales for the week ended January 23, 1954, were 2 percent more than sales in the preceding week and were 1 percent more than sales in the corresponding week last year.

## PRICES

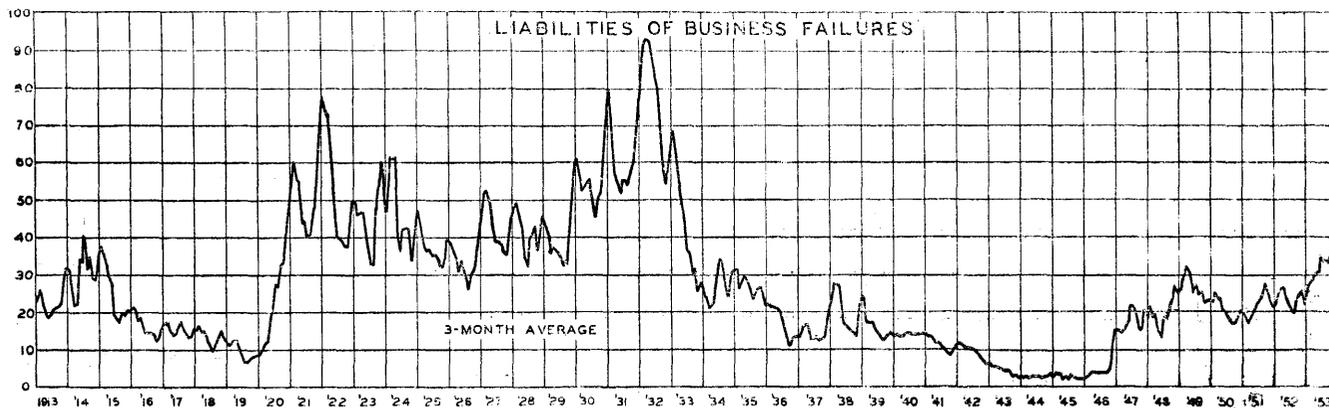
### *Consumers' Prices*

The consumers' price index published by the Bureau of Labor Statistics decreased slightly during the month ended December 15 for the second consecutive month. The December figure was less than one-half of 1 percent below the alltime high reached during October. The index virtually leveled off during 1953.

Primarily responsible for the December decrease of the index of consumers' prices was a slight decrease in apparel prices and a 1-percent decrease in the cost of transportation. The cost of reading and recreation and that of housing remained unchanged; the indices of the four remaining major components of the index increased slightly during the month.

Food prices, which had decreased during each of the 3 months beginning with September, have recovered slightly but the December food index was more than 1 percent below that of December 1952. According to the Bureau of Labor Statistics, seasonal increases of prices for fruits and vegetables and higher pork prices more than offset decreases in prices of eggs, poultry, fish, and meats other than pork. The recent increase of coffee prices was not reflected in the December index.

Costs of medical care, which have been increasing steadily, continued to increase in December. The fact that the December index is 30 percent above that for January 1947 directs attention to an interesting development of recent years. With the ending of controls after World War II, prices of food, apparel, and house-furnishings, all of which are commodities, rose rapidly; rents, which remained under controls, gas and electricity costs, and prices of other goods and services, all of which may be considered somewhat more closely related to services rather than commodities, rose relatively slowly. However, since January 1947, prices of food, apparel,



and housing costs other than rent have risen much less than rents, transportation costs, medical-care costs, and prices of other goods and services.<sup>1</sup>

The expected continuation of the downward trend of general business activity probably will exercise further pressure on consumer prices during the next few months. Of course, the various components of the index may move in somewhat different ways; some may even continue to increase for a few months. Much will depend on the duration and magnitude of the present recession. Moreover, as we pointed out in our last article, there seem to be more institutional rigidities in the marketing structure today than ever before. After consideration of the over-all situation, we believe that, in spite of temporary interruptions, the more probable course of the index of consumers' prices during the next several months will be downward.

### Commodities at Wholesale

	1953		1954
(August 1939=100)	Jan. 28	Jan. 21	Jan. 27
Spot-Market Prices (22 basic raw materials)	273	267	267
Commodity Futures Prices (Dow-Jones Daily Index)	350	355	356

## BUSINESS

### The Trend of Business Failures

The series shown on the accompanying chart is a 3-month moving average (plotted at the midmonth) of liabilities of business failures.<sup>2</sup> The November average increased 9 percent to a post-World War II high. The November figure was 22 percent above that for March 1949, the highest level of failures reached during the 1948-49 recession. Since the 1952 low reached in August the average has risen nearly 100 percent. The November average was the largest since May 1933.

Liabilities of business failures, which had decreased slightly during November, increased 19 percent during December. December failure liabilities were 87 percent greater than those of December 1952. Liabilities

during December totaled \$43,754,000, compared with \$36,795,000 during November and \$23,400,000 during December 1952. The figure was the largest for a December since the 1934 figure of \$45,200,000.

The number of failures was 813 during December, compared with 815 during November and 583 during December a year earlier. Average liabilities per failure increased substantially to \$53,818 from \$45,147 during November. The 1953 record was \$55,014 during July. Business-failure liabilities for 1953 totaled \$394,153,000, compared with \$283,284,000 for 1952. The number of failures was 8,862 in 1953, compared with 7,601 in 1952. Average liabilities per failure were \$44,478 in 1953, compared with \$37,269 in 1952.

The number of failures reported by Dun & Bradstreet for the 3 weeks ended January 21 was 610, compared with 628 during the corresponding weeks of December.

A comparison of recent developments with those during 1948 is of interest. During November of 1948 a peak of general business activity was reached. As we pointed out in our last Monthly Bulletin, we believe that another peak of general business activity occurred during the third quarter of 1953. Thus, in 1948 the 3-month moving average of liabilities of business failures reached a trough 5 months prior to the peak of general business activity; this time, the average reached a trough 13 or 14 months prior to the peak of general business activity.<sup>3</sup> The upward trends of the series in both 1948-49 and thus far in 1952-53 have been similar, even to the extent of both having two temporary interruptions. The increase from the low in 1948 to the high in 1949 was \$18,800,000; the increase from the low in 1952 to the high thus far in 1953 has been \$19,500,000.

The downturn of the series in April 1949 preceded an upturn in general business activity that actually began in October 1949. We believe that a similar downturn at this time will be one of the first indications that a recovery in the not too distant future is probable. A further increase might well be an indication that the recession is to be somewhat more prolonged and severe than that during 1948-49. This series should be watched closely by those attempting to judge business trends, because this has been one of the more reliable of the leading indicators.

<sup>1</sup>Exceptions among the service components of the index are costs of personal care, which have increased about as much as have food prices, and costs of reading and recreation, which have increased somewhat less than have prices of foods.

<sup>2</sup>Failures data are compiled by Dun & Bradstreet, Inc., and include discontinuances following assignment, voluntary or involuntary petition in bankruptcy, attachment, execution, foreclosures, and voluntary withdrawal from business with known losses to creditors.

<sup>3</sup>We have mentioned on previous occasions that the inverted seasonally adjusted monthly series of liabilities of business failures is one of the earliest and most consistent indicators of cyclical changes of business activity; the series usually leads cyclical peaks of general business activity by an average of nearly 11 months.